No. 89-1283

Supreme Court, U.S.
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In the Supreme Court of the United States

OCTOBER TERM, 1989

ARCADIA, OHIO, ET AL., PETITIONERS

v.

OHIO POWER COMPANY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT

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QUESTION PRESENTED

Whether Section 318 of the Federal Power Act (16 U.S.C. 825q), which governs "Conflicts of jurisdiction" between the Federal Energy Regulatory Commission (FERC) and the Securities and Exchange Commission (SEC), precludes FERC jurisdiction whenever the FERC and the SEC have jurisdiction to regulate the same subject matter, or only when there is an actual conflict between a requirement of the FERC and a requirement of the SEC.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-28a) is reported at 880 F.2d 1400. The opinion of FERC (Pet. App. 31a-67a) is reported at 39 F.E.R.C. (CCH) ¶ 61,098. The opinion of FERC denying rehearing (Pet. App. 68a-73a) is reported at 43 F.E.R.C. (CCH) ¶ 61,046.

JURISDICTION

The court of appeals entered its judgment on July 28, 1989. Rehearing petitions filed by FERC and petitioners were denied on October 12, 1989. Pet. App.

29a-30a. On January 2, 1990, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including February 9, 1990, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Public Utility Act of 1935, ch. 687, 49 Stat. 803, had "two primary and related purposes: to curb abusive practices of public utility companies by bringing them under effective control, and to provide effective federal regulation of the expanding business of transmitting and selling electric power in interstate commerce." *Gulf States Utilities Co.* v. *FPC*, 411 U.S. 747, 758 (1973). The Act was divided into two titles, administered by two separate agencies, to achieve these purposes. This case raises the issue of the circumstances under which the regulatory regime created by one title supersedes the regime created by the other.

Title I of the Act contained the Public Utility Holding Company Act (PUHCA), 15 U.S.C. 79 *et seq.*, which subjected public utility holding companies to regulation by the SEC. One of the principal remedial purposes of PUHCA was to protect investors and consumers by preventing public utility holding companies and their subsidiaries from paying or receiving unjustified prices for goods or services due to "an absence of arm's-length bargaining or from restraint of * * * competition." 15 U.S.C. 79a(b)(2). To this end, Section 13(b) of PUHCA, 15 U.S.C. 79m(b), makes it unlawful for affiliates of a public utility holding company to contract with each other:

> except in accordance with such terms and conditions and subject to such limitations and prohibitions as the [SEC] by rules and regulations or order shall prescribe as necessary or appropriate in the public interest or for the protection of investors or consumers and to insure that such contracts are performed economically and efficiently for the benefit of such associate companies at cost, fairly and equitably allocated among such companies.

The SEC has adopted rules implementing this standard. SEC Rule 90 prohibits associated companies from making or performing contracts for sale of goods or performance of services "at more than cost." 17 C.F.R. 250.90(a)(2). The sale between affiliates of seller-produced goods is not "limited to cost," 17 C.F.R. 250.90(d), but such a seller still may not charge its affiliate more than a fair market price. 17 C.F.R. 250.92(b). The net effect of these rules is that, in the absence of an SEC order governing a transaction, seller-produced goods must generally be sold at the lower of cost or market.

Title II of the Public Utility Act of 1935 enacted Part 2 of the Federal Power Act (FPA), 16 U.S.C. 824 *et seq.* These provisions authorized the Federal Power Commission (the predecessor to FERC, see 42 U.S.C. 7172(a)(1)(B), 7293) generally to regulate wholesale electric rates charged by public utility operating companies in interstate commerce in order to ensure that such rates are "just and reasonable." 16 U.S.C. 824d.

Section 213 of the Public Utility Act of 1935, now Section 318 of the FPA, 16 U.S.C. 825q, was designed to govern conflicts between the potentially overlapping authority granted to the two agencies. Entitled "Conflict of jurisdiction," this provision essentially provides for SEC precedence in cases of conflict: "If, with respect to the issue, sale, or guaranty of a security, * * * or the acquisition or disposition of any

security, capital assets, facilities, or any other subject matter, any person is subject both to a requirement of [the PUHCA] * * * and to a requirement of [the FPA], the requirement of [the PUHCA] shall apply to such person, and such person shall not be subject to the requirement of [the FPA] * * * with respect to the same subject matter." Section 318 permits the SEC to exempt a firm subject to requirements under both the PUHCA and the FPA from the PUHCA provision, thus making the FPA provision applicable. 16 U.S.C. 825q.[1]

2. This case arose out of a rate increase proposal that Ohio Power, a utility operating subsidiary of American Electric Power Company, Inc., filed with FERC in 1982 pursuant to Section 205 of the FPA, 16 U.S.C. 824d. In the proceedings that resulted from the Ohio Power filing, certain parties challenged Ohio Power's pass-through to its ratepayers of the price

[1] The complete text of Section 318 is:

Conflict of jurisdiction. If, with respect to the issue, sale, or guaranty of a security, or assumption of obligation or liability in respect of a security, the method of keeping accounts, the filing of reports, or the acquisition or disposition of any security, capital assets, facilities, or any other subject matter, any person is subject both to a requirement of the Public Utility Holding Company Act of 1935 [15 U.S.C. 79 et seq.] or of a rule, regulation, or order thereunder and to a requirement of this chapter or of a rule, regulation, or order thereunder, the requirement of the Public Utility Holding Company Act of 1935 shall apply to such person, and such person shall not be subject to the requirement of this chapter, or of any rule, regulation, or order thereunder, with respect to the same subject matter, unless the Securities and Exchange Commission has exempted such person from such requirement of the Public Utility Holding Company Act of 1935, in which case the requirements of this chapter shall apply to such person.

that it had paid to its subsidiary, the Southern Ohio Coal Company (SOCCO), for coal purchased from SOCCO. Pursuant to a contract between Ohio Power and SOCCO, the price was based on SOCCO's costs.

In 1971, Ohio Power, as part of a public utility holding company system, had required authority from the SEC to undertake certain activities. Acting on an application to create SOCCO as a coal-mining subsidiary, the SEC provided in its order that "[t]he charges for coal by [SOCCO] will be based on an amount equal to the actual cost of [SOCCO] in developing the reserve and mining such coal, including all appropriate overheads and interest charges and including a reasonable rate of return on Ohio Power's equity investment in [SOCCO]." *In re Ohio Power Co.*, SEC Holding Co. Act Release No. 17383, at 2 (Dec. 2, 1971); see Pet. App. 21a. In three subsequent orders authorizing further financing for SOCCO's mining operations, the SEC had stated that the price at which SOCCO coal would be sold to Ohio Power would "not exceed the cost" to SOCCO. *In re Ohio Power Co.*, SEC Holding Co. Act Release No. 20515, 14 SEC Dkt. 928, 929 (Apr. 24, 1978); *In re Southern Ohio Coal Co.*, SEC Holding Co. Act Release No. 21008, 17 SEC Dkt. 310, 312 (Apr. 17, 1979); *In re Southern Ohio Coal Co.*, SEC Holding Co. Act Release No. 21537, 19 SEC Dkt. 1309, 1309 (Apr. 25, 1980).

Ohio Power contended that the four SEC orders had approved its contract to purchase the coal "at cost" from SOCCO pursuant to Section 13 of the PUHCA. Therefore, according to Ohio Power, Section 318 barred FERC from allowing rate recovery of a lesser amount than the cost-based price specified in the SEC-approved contract.

Following an investigation initiated by FERC under Sections 205 and 206 of the FPA, FERC concluded that Section 318 did not bar it from prohibiting the pass-through of any excessive payment Ohio Power had made to its affiliate SOCCO for the "captive" coal. As the Commission viewed it, while PUHCA authorizes the SEC to approve contracts for affiliate sales at cost, that statute did not bar FERC, which operates under a statutory mandate to protect ratepayers from excessive charges, from prohibiting the pass-through in rates of any portion of a utility's coal costs that are not just and reasonable in light of market conditions.

The Commission found that this approach was particularly warranted in this case, since the evidence showed that Ohio Power had paid SOCCO about 25-33% over prevailing market prices for coal during the period from 1982-1986. Pet. App. 58a-59a.[2] FERC therefore ordered Ohio Power to refund the difference; pursuant to that directive, Ohio Power has refunded $13.4 million (of which it still disputes $3.4 million) to its wholesale customers.

3. A divided panel of the D.C. Circuit granted Ohio Power's petition for review and reversed FERC's decision. Interpreting Section 318 *de novo*,[3] the panel majority ruled that "[t]he price term of sales con-

[2] The Commission also found that Ohio Power had paid SOCCO "50% above market in 1980 [and] 94% in 1981," the two years before the initiation of the proceedings before FERC. Pet. App. 58a.

[3] The court initially determined that since Congress had designed Section 318 to allocate jurisdiction between FERC and the SEC, Section 318 could not be deemed "entrusted to FERC's administration" and accordingly FERC's interpretation of Section 318 was not entitled to deference. Pet. App. 8a.

tracts between associated companies are [*sic*] subject to SEC jurisdiction under PUHCA * * * and are [*sic*] therefore a 'subject matter' * * * if such price term is also subject to the requirements of the FPA." Pet. App. 9a. Because, in the court's view, the FERC order at issue "set * * * a different price term for such a contract" (*ibid.*), "[t]he conclusion that the same subject matter is implicated is inescapable." Pet. App. 9a-10a.

Having held that the SEC and FERC regulated the "same subject matter," the court went on to hold that this conclusion alone was sufficient to bar FERC's jurisdiction under Section 318. Pet. App. 14a-16a. FERC had argued that, even if the same subject matter were being regulated by both FERC and the SEC, the "requirements" set by both agencies were consistent. The applicable SEC rules and orders were alleged to have referred to cost as only a ceiling price —not an actual price—for the coal contract between Ohio Power and SOCCO. Because the market price of coal relied upon by FERC was lower than the cost of coal as determined under SEC rules, FERC argued that there was no conflict between the FERC rule requiring market-based pricing and the SEC rule allegedly setting cost as a ceiling price. See FERC C.A. Br. at 23-28.

The court held that this argument proceeded from a "false premise." Pet. App. 14a. The court held that Section 318 preempts FERC so long as FERC in effect attempts to regulate the same subject matter as the SEC, even if the FERC order and the SEC regulation pose no actual conflict. As the court stated, "The fact that FERC's market approach produces a current result that does 'not exceed' cost * * * does not make [Ohio Power] any less subject to section 13(b) or to the SEC's orders." Pet. App. 14a.

In an opinion concurring in the judgment, Judge Mikva disagreed with this latter holding. Judge Mikva noted that, because Section 318 speaks in terms of conflicting "requirements" of FERC and the SEC, FERC is divested of jurisdiction under Section 318 only where the "requirements" the SEC and FERC seek to impose are in actual conflict. Pet. App. 19a-22a. He concluded that "because * * * the SEC's orders * * * permit Ohio Power to pay less than cost for coal, FERC's imposition of a market price less than cost does not in this case create a jurisdictional conflict." Pet. App. 23a.[4]

The court of appeals denied petitions for rehearing and suggestions for rehearing *en banc* filed by FERC and petitioners. Pet. App. 29a. Noting that he would have granted the petition for rehearing by the panel, Judge Mikva filed a statement reemphasizing his view that "the statutory interpretation engaged in by the majority * * * generates a no-man's land where neither the [SEC] nor FERC will patrol holding company practices which can oppress consumers, investors and the public." Pet. App. 30a.

REASONS FOR GRANTING THE PETITION

The D.C. Circuit's decision essentially applied a broad "field preemption" analysis to the overlapping FERC/SEC jurisdiction created by the Public Utility

[4] Judge Mikva nonetheless agreed with the majority that the FERC order had to be vacated. In his view, FERC's Rule 35.14(a)(7) (18 C.F.R. 35.14(a)(7)) barred the Commission from imposing a market-price test. Pet. App. 23a-28a. In discussing Rule 35.14(a)(7) in its own decision, FERC had held that it merely "creates a presumption of reasonableness, not a conclusive finding of reasonableness" with respect to pricing at cost. Pet. App. 41a. The majority did not discuss this issue.

Act of 1935. Under the court's analysis, if the SEC has taken any regulatory steps with respect to a given subject matter—or even if the statute grants the SEC authority to take such steps—FERC is apparently precluded from any form of regulation of that subject matter. This interpretation of Section 318 is in substantial tension with settled judicial precedent and the language and legislative history of Section 318. It threatens considerable interference with the proper and efficient allocation of jurisdiction between the FERC and the SEC and creates the potential for a serious regulatory gap with respect to federal (and by implication state) regulation of utility rates. For these reasons, and because the view of FERC, as an agency responsible for administering the Public Utility Act of 1935, is entitled to substantial deference with respect to the question presented in this case, see *Chevron USA Inc.* v. *NRDC*, 467 U.S. 837 (1984), we support the petition for a writ of certiorari. See Sup. Ct. R. 12.4.

1. The D.C. Circuit's decision is in substantial tension with the holding of the Fourth Circuit in *Appalachian Power Co.* v. *FPC*, 328 F.2d 237, cert. denied, 379 U.S. 829 (1964), that Section 318 requires a much more focused "actual conflict" analysis. *Appalachian Power* involved a claim by a power company that, because the FPC and the SEC had both prescribed accounting rules for it, Section 318 excused it from compliance with the FPC requirements. The Fourth Circuit expressly held that "[u]nder section 318 of the Federal Power Act * * * *actual conflicts* between the FPC and the SEC are resolved in favor of the SEC." 328 F.2d at 250 (emphasis added). After a careful analysis of the accounting rules at issue, the court concluded that, although both agencies prescribed accounting rules, the two sets of rules were

not inconsistent. Therefore, the court held that "the effort to discover an *incompatibility* between the two governmental agencies must fail." *Id.* at 252 (emphasis added). The court's ruling that Section 318 did not divest the FPC of jurisdiction unless an "actual conflict" or "incompatibility" between FPC and SEC regulation were shown is inconsistent with the result reached by the D.C. Circuit in this case.

In reaching its conclusion that an actual conflict analysis is appropriate under Section 318, the Fourth Circuit relied on this Court's decision in *Northwestern Elec. Co.* v. *FPC*, 321 U.S. 119 (1944).[5] In *Northwestern*, a holding-company utility argued that, although there was no present conflict between the SEC's and the FPC's accounting requirements, the authority of the SEC to impose accounting requirements generally preempted the FPC under Section 318 from imposing accounting requirements of its own. The Court rejected the preemption claim on the ground that "no conflict" existed between the FPC's requirements and those of the SEC. 321 U.S. at 125. Although the Court's brief discussion of the issue in *Northwestern* occupies only a single paragraph, the result in *Northwestern* also suggests that the D.C.

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[5] The Fourth Circuit also relied on a letter from the Chairman of the SEC to the Solicitor General that was made a part of the record in *Northwestern*. In a portion of that letter not quoted in the Fourth Circuit's decision, the SEC explained:

> Section 318 of the Public Utility Act of 1935 resolves the question of possible conflicting requirements * * *. Until the S.E.C. does by rule or order impose 'requirements' * * *, there can be no conflict of requirements and Sec. 318 does not apply. It was not intended that utility companies should be able to thwart regulation by the F.P.C. by conjuring up under Sec. 318 imaginary conflicts with *potential* action of the S.E.C.

Resp. Br. App. D at 98-99, *Northwestern Elec. Co.* v. *FPC*, 321 U.S. 119 (1944).

Circuit erred in rejecting an "actual conflict" approach.

2. The field preemption analysis used by the D.C. Circuit originated in cases involving state regulation of an area that Congress had intended be regulated by the federal government. See, *e.g.*, *Schneidewind* v. *ANR Pipeline Co.*, 108 S. Ct. 1145, 1150-1156 (1988). However, even in the federal/state context, "field pre-emption" is applied only where it can be determined that Congress intended an articulated federal regulatory scheme to "occupy a given field to the exclusion of state law." *Id.* at 1150. In other cases, in which no such congressional intent can be shown, state regulation is found incompatible with a federal regulatory scheme only if there is an actual conflict between a requirement of the state scheme and the federal regulations. See, *e.g.*, *Northwest Central Pipeline Corp.* v. *State Corp. Comm'n*, 109 S. Ct. 1262, 1273-1278 (1989).

The Public Utility Act of 1935 expressly granted regulatory jurisdiction to FERC and the SEC—two *federal* agencies. Although Section 318 certainly demonstrates Congress's intent that SEC regulation should take precedence over FERC regulation, the statute also manifests an intent to permit both agencies to regulate matters that are very closely related. This fact alone suggests that a court should be extremely cautious before concluding, as the court of appeals did, that the mere existence of SEC jurisdiction over a subject matter ousts FERC entirely from the field. Other factors make it clear that a broad field preemption analysis is inappropriate for use in the Section 318 context.

First, the plain language of Section 318 strongly suggests that an actual conflict is necessary. Section 318 itself is entitled "Conflict of jurisdiction," suggesting a recognition that overlapping authority has

been conferred on the two agencies. Moreover, Section 318 gives the SEC precedence only when an entity is subject to "a *requirement* of [the PUHCA] and a *requirement* of [the FPA]" with respect to the same subject matter (emphasis added). Regulatory action permitting a regulated entity to perform any one of a range of permissible actions would not impose a *requirement* at conflict with action by the other agency compelling the regulated entity to take one of the permissible actions. Imposition of inconsistent requirements by both agencies is necessary before Section 318's rule of SEC precedence takes effect.

The legislative history of Section 318 similarly emphasized conflicts in the exercise of jurisdiction, not merely overlapping authority. As the Conference Report explained in regard to Section 318 (H.R. Rep. No. 1903, 74th Cong., 1st Sess. 75 (1935) (emphasis added)):

> In Subsection (a) of Section 318, in which *conflicts* of jurisdiction between the Securities and Exchange Commission and the Federal Power Commission under this bill are resolved in favor of the former, the House amendment adds to such *matters of conflict* the assumption of obligation or liability in respect of a security. The conference substitute is enlarged to include any *conflict arising under* this bill.

Similarly, Section 21 of the PUHCA, 15 U.S.C. 79u (emphasis added), explicitly provides that nothing in the PUHCA "shall affect the jurisdiction of any other commission * * * of the United States * * * insofar as such jurisdiction does not *conflict* with any provision of [the PUHCA] or any rule, regulation, or order thereunder."

Second, use of the broad field preemption analysis to govern the relationship between FERC and the SEC could create a substantial regulatory gap, defeating Congress's intent by leaving transactions effectively unregulated by either agency. It is important to stress that the court of appeals in this case did not simply interpret SEC orders to require Ohio Power to pay cost to SOCCO, and then hold that an actual conflict between the SEC orders and FERC existed.[6] Rather, the court held that, under Section 13(b) of PUHCA, "[i]n the absence of exemption, it is for the SEC rather than FERC to determine the inter-associate price." Pet. App. 14a. Thus, FERC is apparently ousted of power with respect to any "subject matter" that may arise under both the PUHCA and the FPA, notwithstanding the fact that the SEC may have never acted at all with regard to that subject matter. This threatens to create regulatory gaps far beyond the matters at issue in this case or, indeed, the subject matters governed by Section 13(b).[7]

3. Finally, the importance of the question presented is underscored by the potential rate impact on Ohio Power's customers in this case. As noted above, Ohio Power paid its affiliate 25-33% over prevailing market prices for coal during 1982-1986, and over

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[6] Because the court of appeals did not reach the issue of whether in fact the SEC and FERC orders imposed conflicting requirements in this case, that issue would be open on remand.

[7] Indeed, one of the principal goals of the Public Utility Act of 1935 was to eliminate the regulatory gap that existed at that time because, in *Public Util. Comm'n* v. *Attleboro Steam & Elec. Co.*, 273 U.S. 83, 86-90 (1927), this Court had held that certain sales of electricity were in interstate commerce and thus beyond the reach of state regulation. See *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982). See generally Note, *Federal Regulation of Holding Companies: The Public Utility Act of 1935*, 45 Yale L.J. 468 (1936).

50% above market in 1980 and 94% in 1981. Petitioners reasonably catalogue the potentially far-reaching consequences of a decision that could hinder effective regulation of utilities that directly or indirectly serve 49 million households in 30 states and the District of Columbia. Pet. 17-18.[8]

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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[8] Judge Mikva's conclusion, in concurring in the result reached below (see Pet. App. 30a) that FERC's own regulation barred it from applying a market-based test to Ohio Power's coal purchases from SOCCO ought not deter the Court from granting the petition. Since the majority did not address the meaning of the FERC regulation on which Judge Mikva relied, the interpretation of that regulation would remain open on remand. FERC has argued both in its brief to the panel and in its petition for rehearing that the regulation creates no such bar to the action taken in this case. See C.A. Br. 30-32; C.A. Pet. for Rehearing 12-14.

* The Solicitor General is disqualified in this case.

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